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In The

SUPREME COURT OF THE UNITED STATES

October Term, 1995

PHILIP MORRIS INCORPORATED,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF UNISYS CORPORATION AS AMICUS CURIAE IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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Unisys Corporation files this brief amicus curiae in support of the petition for writ of certiorari filed by Philip Morris Incorporated. Unisys is a multinational corporation presently engaged in a controversy with the Internal Revenue Service regarding the proper tax treatment of income realized

on the repayment of certain foreign currency borrowings entered into in the ordinary course of its business. One of the issues involved in that controversy is the issue presented in the instant case.[1/]

REASONS FOR GRANTING THE WRIT

Unisys strongly urges this Court to resolve the conflict between the Second Circuit decision below and the Sixth Circuit decision in Kentucky & Indiana Terminal R.R. v. United States, 330 F.2d 520 (6th Cir. 1964). Taxpayers had consistently relied on Kentucky & Indiana in determining the tax consequences of income realized on the repayment of foreign currency borrowings. At no time prior to the decision of the Tax Court in the instant case was there any indication that Kentucky & Indiana would not govern the issue here presented.

Nothing in United States v. Centennial Savings Bank FSB, 499 U.S. 573 (1991), indicates the slightest focus by this Court on the unique tax treatment accorded transactions involving foreign currency. A decision that considered only the taxability of penalty income realized by a bank on the early withdrawal of a domestic certificate of deposit should not, without more, be controlling in the far different and considerably more complex realm of foreign currency transactions.

In its petition for certiorari, Philip Morris points out the illogic of allowing Centennial Savings Bank to control the outcome of the instant case. A U.S. taxpayer is required to

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[1/] Both petitioner and respondent have consented to the filing of this brief in letters lodged with the Clerk of this Court.

treat a borrowing of foreign currency as if it were a borrowing of U.S. dollars. That is why income may be realized on repayment even though the exact amount of foreign currency borrowed is repaid. To deny the taxpayer the benefit of tax deferral in such a case simply because, for business reasons, it in fact borrowed foreign currency rather than U.S. dollars directly is not only arbitrary but also contrary to the purpose for which I.R.C. section 108(a) was enacted.

Surely Congress did not intend that the IRS could have it both ways -- requiring the taxpayer to use a dollar-based calculation to determine whether any income was realized on repayment of the debt, but a foreign currency-based calculation to determine whether any such income was eligible for tax deferral. If the IRS is correct and the number of currency units repaid is to determine eligibility for tax deferral, then the number of currency units repaid should also determine whether there is income in the first instance. If 100 million Swiss francs are borrowed and 100 million Swiss francs are repaid, it would be quite logical to conclude that there was no income at all as a result of the repayment. See B.F. Goodrich Co. v. Commissioner, 1 T.C. 1098 (1943), a case reaching that conclusion but not followed in later decisions.

As the petition for certiorari makes clear, Congress sought through section 108(a) to encourage the repayment of debt when a debtor had the opportunity to pay off its obligations at less than face value. Since repayment would give rise to taxable income in those circumstances under the rule of United States v. Kirby Lumber Co., 284 U.S. 1 (1931), Congress undertook to provide relief in the form of

tax deferral. Otherwise, the transaction would trigger a current tax that would require an additional cash outlay. Taxpayers might then find themselves unwilling or unable to take advantage of the opportunity to repay their debts at a discount even though, from an economic point of view, it would be desirable to do so.

The petition for certiorari also points out the inconsistency between this Court's holdings in Centennial Savings Bank and Kirby Lumber Co. If Centennial Savings Bank is read literally, it would appear that even a debtor similar to the debtor involved in Kirby Lumber Co. would not qualify for the benefit of section 108(a). But this Court took pains in Centennial Savings Bank to show that Kirby Lumber Co. was consistent with its interpretation of the statute. That being the case, a literal application of Centennial Savings Bank -- which the Second Circuit adopted below -- cannot be required in those situations where, as here, negotiating a creditor's release makes no sense.

Unisys believes that if a Kirby Lumber type of situation is intended to be within the scope of section 108(a), as it clearly is, the courts below have misapplied this Court's holding in Centennial Savings Bank. It is clear from the opinion of the Second Circuit that, but for a literal application of Centennial Savings Bank, section 108(a) would have been available to petitioner here, as a borrower of foreign currency that took advantage of market conditions and repaid its debt when the dollar value of the currency had declined. Since a borrower of foreign currency must account for the transaction in dollar terms, it is completely inappropriate to ignore the dollar aspects of the transaction in

determining whether the borrower is entitled to tax deferral with respect to the income realized on repayment.

At a minimum, Centennial Savings Bank has severely muddied the waters in this area. A clarification of the scope of section 108(a) has therefore become essential to permit a proper resolution of pending tax audits without continuing controversy.

CONCLUSION

For all of the foregoing reasons, Unisys respectfully urges this Court to grant the petition for writ of certiorari.

Respectfully submitted,

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